State of California

Board of Equalization

Legal Department-MIC: 82

## Memorandum

305.0012

To: Janice L. Thurston Date: December 17, 2003

**Assistant Chief Counsel** 

From: Carla J. Caruso Telephone: (916) 324-2816

Senior Tax Counsel CalNet: 8-454-2816

Subject: F.O.B. Shipment by Mail or Common Carrier to

**Indian Reservations** 

This memorandum is in response to your request for clarification of shipping requirements for deliveries by mail or common carrier, including F.O.B. delivery terms, in order for an off-reservation retailer to have a sale of goods to an Indian purchaser take place on a reservation. We have recently addressed this issue in two opinion letters dated July 7, 2003, and July 11, 2003, respectively (copies attached). These letters analyze the requirements of Regulation 1616(d)(4)(A) regarding the application of tax, together with the expanded title passage requirements set forth in Regulation 1628(b)(3)(D), including F.O.B. delivery terms.

In these letters, we conclude that unless shipment is by facilities of the retailer, in order to comply with the requirements of Regulation 1616(d)(4)(A) that title *and* possession of the goods actually pass to the Indian purchaser on the reservation, the contract of sale (or a document reflecting that contract issued contemporaneously with the sale, such as the retailer's invoice), must include a statement expressly requiring delivery on the reservation, e.g., one of the contract terms is F.O.B. the reservation, and cannot include a provision passing title prior to that time. (Reg. 1628(b)(3)(D).) Moreover, the goods must *in fact* be delivered to the Indian purchaser on the reservation, and the transportation documents, such as any bill of lading, must state that delivery is at destination, e.g., F.O.B. the reservation. (See *ibid.*, Reg. 1616(d)(4)(A).) As we explain, agreement by the parties that title is to pass on the reservation is insufficient for the sale to occur on the reservation when the goods are shipped by mail or common carrier, unless additional requirements are met.

We reached this conclusion based upon the following analysis.

First, with regard to sales by off-reservation retailers, Regulation 1616(d)(4)(A) provides that when a retailer makes a sale of tangible personal property to an Indian negotiated at a place of business off a reservation, that sale is not subject to tax if the delivery (transfer of

possession)<sup>1</sup> is made to the Indian purchaser on a reservation and title (ownership) transfers to the purchaser on a reservation. That subdivision further explains that generally, title (ownership) to the property transfers upon delivery if delivery is made by facilities of the retailer, and ownership transfers upon shipment if delivery is made by mail or carrier. (*Ibid.*) On the other hand, if the property is delivered off the reservation *or* the ownership transfers to the purchaser off the reservation, the sale is subject to tax. (*Ibid.*)

Second, Regulation 1628, consistent with California Uniform Commercial Code section 2401, sets forth an expanded discussion of where a sale takes place. Subdivision (b)(3)(D) of Regulation 1628 explains that unless explicitly agreed that title is to pass at a *prior* time, the sale occurs at the time and place at which the retailer completes his or her performance with reference to the physical delivery of the property.

In other words, the parties may agree that title is to pass *prior* to physical delivery, and in such case the sale takes place at that time, even though physical delivery takes place later. (Cf. Rev. & Tax. Code, § 6006, providing that sale means and includes any transfer of title or possession of tangible personal property for a consideration.) However, in the absence of the parties' agreement that title is to pass at a *prior* time, the sale occurs when and where the retailer completes its obligations regarding delivery. Thus, when the parties do not agree that title is to pass before delivery, the time and place of sale are determined by the time and place of delivery. The time and place of delivery, in turn, are determined by whether the parties have agreed to delivery terms, and, if so, the terms and manner of delivery to which the parties agree.

Regulation 1628(b)(3)(D) explains that if the contract of sale requires or authorizes the retailer to send the property to the purchaser but does not require him or her to deliver it at destination, the retailer completes his or her performance with reference to the physical delivery of the property at the time and place of shipment (unless shipment is by facilities of the retailer), for example, when the property is delivered to the shipper for delivery to the customer. On the other hand, "if the contract [of sale] expressly requires *delivery* at destination, including cases where one of the terms of the contract is F.O.B. place of destination, the retailer completes his performance with reference to the physical delivery of the property on tender to the purchaser there." (*Ibid.*; emphasis added.)

Therefore, in circumstances where delivery is *not* by the facilities of the retailer, we concluded that in order to fulfill the requirements of Regulation 1616(d)(4)(A) that title *and* possession of the materials actually pass to the Indian purchaser on the reservation (1) the contract of sale (or a document reflecting that contract issued contemporaneously with the sale, such as the retailer's invoice) must include a statement expressly requiring delivery on the reservation, e.g., one of the contract terms is F.O.B. the reservation (Reg. 1628(b)(3)(D)); (2) title must not pass prior to that time (*ibid*.); and (3) the goods must *in fact* be delivered to, and title (ownership) must pass to, the Indian purchaser on the reservation, and thus transportation

<sup>1</sup> See, e.g., Black's Law Dictionary (7<sup>th</sup> ed. 1999) p. 440, which defines "actual delivery" as "[t]he act of giving real and immediate possession to the buyer or the buyer's agent."

documents, such as any bill of lading, must designate that delivery is at destination, e.g., F.O.B. destination. (*Ibid.*; Reg. 1616(d)(4)(A).)

Staff has raised the issue of whether an off-reservation retailer fulfills Regulation 1616(d)(4)(A)'s requirements that title and possession transfer to the Indian purchaser on the reservation, when the retailer and Indian purchaser agree in the contract of sale or equivalent document that title is to pass to the purchaser on the reservation, and the goods are shipped to the reservation via mail or common carrier. As we indicated above, the answer is no, unless the shipping documents also state that the goods are F.O.B. the destination. As we have explained, Regulation 1628(b)(3)(D), consistent with California Uniform Commercial Code section 2401, allows the parties to agree in the contract of sale to transfer title prior to delivery. However, absent an agreement to pass title prior to delivery, both the Uniform Commercial Code and Regulation 1628(b)(3)(D) mandate that title is in fact transferred, and the sale occurs, when the retailer completes his or her performance with reference to physical delivery. Thus, under Regulation 1628 and Commercial Code section 2401, unless the contract of sale expressly states that delivery is to be on the reservation, i.e., F.O.B. the reservation, the retailer completes his or her performance upon delivery of the property to the shipper for the shipper's delivery to the purchaser. Since title transfers at the time the property is passed to the shipper, the sale occurs off the reservation. Under these circumstances, a title clause, which reserves title in the retailer until delivery to the purchaser, is limited in effect to a security interest in the goods sold. (Cal. Unif. Comm. Code, § 2401(1) and (2).) Accordingly, the seller and the purchaser cannot agree to transfer title on the reservation, because transfer of title has in fact already occurred at the time the goods were transferred to the shipper for delivery to the purchaser.

If the contract of sale does expressly state that delivery is to be on the reservation, i.e., F.O.B. the reservation, under Regulation 1628 and Commercial Code section 2401 title passes on the reservation. However, since Regulation 1616(d)(4)(A) requires that both title and possession pass on the reservation for a sale to be made on the reservation, we require documentation by way of bills of lading or other transportation documents that indicate F.O.B. the reservation, in order to show that possession and title *in fact* passed on the reservation. This requirement is in addition to any agreement in the contract of sale.

In view of the above discussion, we recommend deletion of Sales and Use Tax Annotation 305.0028.900 (6/24/97). That annotation involves the sale of goods to an Indian tribe, but does not discuss the requirements of Regulation 1616(d)(4)(A). We note that Sales and Use Tax Annotation 305.0028.025 (6/12/02), which discusses the requirements of Regulation 1616(d)(4)(A) in the context of a construction contract, is consistent with the analysis we have set forth above. That more recent annotation specifies that in order to fulfill the requirements that title and possession of goods actually pass to the Indian purchaser on the reservation, the contract, invoices, and bills of lading must stipulate that the materials are to be shipped F.O.B. the reservation (unless the goods are delivered by the retailer's own facilities).

I will provide any further information you require after reviewing this memorandum and the attached letters.

CJC:ds Attachments

cc: Mr. Jeffrey McGuire (MIC:92)

Mr. Robert Bergkamp (MIC:44) Ms. Sharon Jarvis (MIC:82)



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### STATE BOARD OF EQUALIZATION

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> RAMON J. HIRSIG Executive Director

April 28, 2005

Ms. T--- -. A---F---, P--- & H---, ------ Plaza XXXX South --- Road, Suite XXX ---, --- XXXXX

Re: CLD 1063—Proposed Annotation 305.0012 (12/17/03); Proposed Deletion of Annotations 305.0028.900 (6/24/97) and 305.0100 (6/13/96).

Dear Ms. A---:

This responds to your letter dated July 12, 2004, to David Rosenthal, Annotations Coordinator, objecting to proposed Sales and Use Tax Annotation 305.0012 (12/17/03), and objecting to the proposed deletion of Sales and Use Tax Annotations 305.0028.900 (6/24/97) and 305.0100 (6/13/96). Your letter was forwarded to the Legal Department for response.

#### You write:

"Our firm represents tribes and individual Indians in California. This letter is provided to object to proposed Annotation 305.0012 as published in Current Legal Digest (CLD) Number 1063. This letter is also provided to request that Annotations 305.0028.900 and 305.0100 not be deleted unless and until the Board of Equalization provides more information about the specific concerns it has about the backup letters including which facts are omitted in order to clarify the Annotations.

"Proposed Annotation 305.0012 is not acceptable as drafted. The proposed Annotation contemplates requiring that all sales contracts between off-reservation retailers and Indian purchasers expressly contain a provision stating 'that delivery is to be on the reservation, i.e., F.O.B. the reservation [.]' In other words, all sales contracts will require a 'F.O.B. the reservation' clause or the sale will not be tax exempt regardless of the circumstances. The requirement is not reasonable and does not appear to be required in analogous situations involving non-Indian purchasers. In addition, if transported by a third party shipper, the 'F.O.B. the reservation' clause would need to be repeated on the 'bill of sale (or equivalent document)' or the bill of lading. These requirements are onerous and impractical.

"The proposed Annotation relies on Regulation 1628(b)(3)(D) and California Commercial Code section 2401 to place these requirements on Indian purchasers and on persons and entities. However, neither Regulation 1628(b)(3)(D) nor California Commercial Code section 2401 require[s] what Annotation 305.0012 is proposing. The provisions of the Code and Regulation allow for title to pass to the buyer 'at the time and place at which the seller completes his performance with reference to the physical delivery of the goods....' Cal. Comm. Code § 2401(2). If the agreement between the non-Indian seller and the Indian purchaser contemplates delivery on the reservation, the contract should not be required to read 'F.O.B. the reservation.' The added requirement of demonstrating through bill of lading or similar document that the title and possession of the goods 'in fact passed on the reservation' and not upon purchase or shipment does not appear to be rooted in either the Code or the Regulation, either.

"While we understand the need for clarity in transactions such as these, we do not agree that Indian purchasers or those who sell to Indians should be expected to do more than others who conduct business off reservation.

"The concerns regarding Annotations 305.0028.900 and 305.0100 are unclear and we believe it is important to explain the concerns more thoroughly prior to deletion of the Annotation[s].

"In sum, proposed Annotation 305.0012 should not be adopted as drafted. In addition, Annotations 305.0028.900 and 305.0100 should not be deleted at this time."

#### Discussion

Annotations are summaries of conclusions of law reached in selected legal opinions of counsel, which do not have the force and effect of law, and which may be revised at any time. (Reg. 5200.)

Initially, we provide additional information concerning the proposed deletion of Annotations 305.0028.900 (6/24/97) and 305.0100 (6/13/96). The letter that is the backup to Annotation 305.0028.0900 does not contain a full discussion of the facts. For instance, the letter that is the backup does not discuss whether there was a bill of lading and if so, whether any information concerning delivery was contained in that bill of lading. Annotation 305.0100 does not specify whether the tribal taxes in question are imposed upon Indian purchasers, and the letter that is the backup to that annotation does not provide that information.

Next, proposed Annotation 305.0012 in Current Legal Digest No. 1063, dated June 13, 2004, states:

**'F.O.B. Shipment by Mail or Common Carrier to Indian Reservation.** An off-reservation retailer contracts with an Indian purchaser for the purchase of tangible personal property. In the contract of sale (or equivalent document) the retailer and the Indian purchaser agree that title is to pass to the purchaser on the reservation and goods are shipped to the reservation via mail or common carrier. Neither the contract of sale nor the shipping documents contains an 'F.O.B. the reservation' clause [or an equivalent clause expressly stating that delivery is to be on the reservation]. Has the retailer fulfilled Regulation 1616(d)(4)(A)'s requirements that title and possession of the property transfer to the Indian purchaser on the reservation?

"Unless the contract of sale expressly states that delivery is to be on the reservation, e.g., F.O.B. the reservation, the retailer completes his or her performance [and title passes to the purchaser] upon delivery of the property to the shipper for the shipper's delivery to the purchaser. (Regulation 1628(b)(3)(D) and Uniform Commercial Code section 2401.) Since title transfers [to the purchaser] at the time the property is passed to the shipper [for the shipper's delivery to the purchaser], the sale occurs off the reservation. Therefore, agreement by the parties that title is to pass on the reservation is insufficient for the sale to occur on the reservation when goods are shipped by mail or common carrier [unless the agreement also expressly states that delivery is to be on the reservation].

"Regulation 1616(d)(4)(A) requires that both title and possession of the goods actually pass to the Indian purchaser on the reservation. When the retailer delivers the property to the reservation by *other* than his or her own facilities, four conditions must be met in order for the transaction to qualify as a [sale] on the reservation. First, the contract of sale (or equivalent document) must include a statement expressly requiring delivery on the reservation. Second, title cannot be passed prior to the time the merchandise is delivered to the Indian purchaser on the reservation. Third, the goods must in fact be delivered to the Indian purchaser on the reservation. Fourth, the transportation documents, such as any bill of lading, must state that delivery is at destination, e.g., F.O.B. the reservation. In other words, the 'F.O.B. the reservation' clause [or an equivalent clause expressly stating that delivery is to be on the reservation] must be included in the bill of sale (or other equivalent document) in order to pass title [and possession] on the reservation, and the clause must also be included in the transportation documents in order to show that [transfer of] title [and possession] in fact occurred on the reservation. This requirement [concerning the bill of lading] is in addition to any agreement in the contract of sale. Since the contract of sale and the transportation documents in the above example did not contain an 'F.O.B. the reservation' clause [or its equivalent], the retailer has not fulfilled the requirements of Regulation 1616. Tax applies to the sale of the property because title in fact transferred to the purchaser when the property was delivered to the shipper for transportation to the reservation. (12/17/03)"<sup>1</sup>

As we understand it, your primary concern is that on-reservation Indian purchasers who buy goods from off-reservation retailers, or those off-reservation retailers who sell goods to on-reservation Indians, should not "be expected to do more than others that conduct business off reservation." By this we assume you mean that Board regulations explaining when a sale occurs, and the manner in which exemptions from tax must be established, should be uniformly applied.

As a starting point, Regulation 1628(b)(3)(D) explains when title passes, and a sale occurs, under circumstances when goods are delivered to the purchaser by carrier or the facilities of the retailer. That subdivision of Regulation 1628 incorporates certain provisions of California Commercial Code section 2401. The regulation and the statute apply to determine when the sale occurs, in instances where goods are delivered to the purchaser by carrier, regardless of whether the purchaser is an Indian, or whether the sale takes place on a reservation. We note that Sales and Use Tax Annotation 325.0088 (9/18/95) discusses the place of sale as set forth in Regulation 1628(b)(3)(D) and Commercial Code section 2401. That annotation, which does not specifically refer to Indian purchasers, states in pertinent part:

"In determining the place of sale, you must first determine if there is a title clause. Unless such a title clause passes title sooner, title passes and the sale occurs when the seller completes its duties with respect to physical delivery of the property (Cal UCC 2401.) When delivery is by the seller's own facilities, the seller completes its duties with respect to physical delivery upon tender of the property to the purchaser. When delivery is by common carrier and the contract states 'F.O.B. destination,' the seller does not complete its duties with respect to physical delivery until the property is delivered at destination. Under such a contract, the sale occurs at destination unless the contract specifically states that title passes sooner. If the contract does not have an F.O.B. destination provision and delivery is by common carrier, the sale occurs upon the seller's tender of the property to the common carrier, unless the contract specifically passes title sooner." (Emphasis added.)

In other words, when goods are delivered by common carrier, the contract of sale *must* contain an F.O.B. destination or equivalent provision in order for the sale to occur at the destination (assuming that the parties have not agreed to transfer title prior to delivery). In the absence of a provision in the contract of sale specifying delivery F.O.B. destination or the equivalent, title to the goods transfers (and the sale occurs) at the time the seller transfers the goods to the common carrier for delivery to the purchaser. Thus, the parties cannot simply agree to transfer title to goods at destination when shipping by common carrier, without including an

<sup>1</sup> Please note that various clarifications have been added (within brackets) to the proposed annotation. These additions are being sent to the Annotations Coordinator as amendments that should be made to the proposed annotation.

F.O.B. destination or equivalent provision in the contract, because without such a provision title will have *already* transferred to the purchaser before the goods arrive at their destination. We note that Regulation 1628(b)(3)(D)'s requirements regarding the place of transfer of title and place of sale apply uniformly to Indian purchasers and non-Indian purchasers whose goods are shipped by common carrier. Thus, Indian purchasers, and the sellers of goods in sales transactions with Indians, are required to meet precisely the same standard as are any other purchasers and sellers in order for a sale to occur and title to transfer of goods shipped by common carrier upon delivery at a shipping destination.

We further note that under Regulation 1628(b)(3)(D), the requirement for an F.O.B. delivery provision in the contract of sale in order for the sale to occur and title to transfer upon delivery to the purchaser applies *only* when the goods are shipped by carrier.<sup>2</sup> If the retailer delivers goods to the purchaser by means of the retailer's own facilities (i.e., its own trucks), title transfers and the sale occurs at the time the retailer delivers the goods to the purchaser unless there is an explicit prior written agreement that title is to pass at another time. This requirement also applies equally to Indian and non-Indian purchasers, and the retailers that sell to them.

Lastly, we note that under Revenue and Taxation Code section 6091, it is presumed that all gross receipts from the sale of tangible personal property are subject to tax. Thus, in order to qualify for an applicable exemption from tax, any retailer must establish that the gross receipts from any claimed exempt sale to any customer are exempt from tax. Accordingly, in order for a retailer to establish that gross receipts from a sale to an Indian purchaser are exempt from tax under Regulation 1616(d)(4)(A), the retailer is required to provide documentation to establish the exemption, including documentation that delivery in fact occurred on the reservation as required by that regulation.

We trust that this responds to your questions. If you have further questions, please feel free to write again.

Sincerely,

Carla J. Caruso Senior Tax Counsel

CJC/ds

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<sup>&</sup>lt;sup>2</sup> We note that the proposed annotation refers *only* to purchases shipped by mail or other common carrier. Accordingly, your statement that "all sales contracts will require a 'F.O.B. the reservation' clause" is inaccurate. <sup>3</sup> As you know, Regulation 1616(d)(4)(A) explains that when a non-Indian retailer makes a sale of tangible personal property to an Indian negotiated at a place of business off a reservation, that sale is not subject to sales tax if the delivery is made to the Indian purchaser on a reservation and title (ownership) transfers to the purchaser on a reservation.

cc: Out-of-State District Administrator (OH) Mr. David Rosenthal (MIC:50)